

**KIVALLIQ ENERGY CORPORATION**

**CONDENSED INTERIM FINANCIAL STATEMENTS**

**FOR THE THREE AND NINE MONTH PERIODS ENDED JUNE 30, 2012**

**Canadian Dollars**

**Unaudited – Prepared by Management**



## **Notice of Non-review of Condensed Interim Financial Statements**

The attached condensed interim financial statements for the three and nine month periods ended June 30, 2012 have been prepared by, and are the responsibility of, the Company's management and have been approved by the Board of Directors of the Company. The Company's independent auditor has not performed a review of these condensed interim financial statements.

**Kivalliq Energy Corporation**  
*(An Exploration Stage Company)*  
**Condensed Statements of Financial Position**

*(Expressed in Canadian Dollars)*  
*Unaudited – Prepared by Management*

<b>ASSETS</b>	<b>Notes</b>	<b>As at June 30, 2012</b>	<b>As at September 30, 2011</b>
<b>Current</b>			
Cash and cash equivalents		\$ 15,012,745	\$ 7,213,622
Other receivables		63,015	467,979
HST recoverable		439,335	931,236
Prepaid expenses		137,108	197,836
		<b>15,652,203</b>	<b>8,810,673</b>
<b>Equipment</b>	<b>3</b>	<b>781,542</b>	<b>574,912</b>
<b>Intangible Assets</b>	<b>4</b>	<b>3,401</b>	<b>5,121</b>
<b>Exploration and Evaluation Assets</b> <i>(Schedule)</i>	<b>5</b>	<b>39,764,157</b>	<b>27,882,471</b>
		<b>56,201,303</b>	<b>37,273,177</b>
<b>LIABILITIES</b>			
<b>Current</b>			
Accounts payable and accrued liabilities		1,898,525	3,901,304
Flow Through Share Premium Liability		196,916	-
		<b>2,095,441</b>	<b>3,901,304</b>
<b>Deferred Tax Liability</b>		<b>4,186,663</b>	<b>2,354,310</b>
		<b>6,282,104</b>	<b>6,255,614</b>
<b>SHAREHOLDERS' EQUITY</b>			
<b>Share Capital</b>	<b>6</b>	<b>52,962,700</b>	<b>30,991,994</b>
<b>Contributed Surplus</b>		<b>6,894,491</b>	<b>5,866,528</b>
<b>Deficit</b>		<b>( 9,937,992 )</b>	<b>( 5,840,959 )</b>
		<b>49,919,199</b>	<b>31,017,563</b>
		<b>\$ 56,201,303</b>	<b>\$ 37,273,177</b>

Nature of Operations and Going Concern *(Note 1)*  
 Commitments *(Notes 5 and 10)*  
 Subsequent Events *(Note 13)*

APPROVED ON AUGUST 24, 2012 ON BEHALF OF THE BOARD:

"James Paterson", CEO, Director

"John Robins", Director

- The accompanying notes are an integral part of these condensed interim financial statements -

**Kivalliq Energy Corporation**  
*(An Exploration Stage Company)*  
**Condensed Statements of Comprehensive Loss**

*(Expressed in Canadian Dollars)*  
*Unaudited – Prepared by Management*

	Notes	Three month periods ended June 30		Nine month periods ended June 30	
		2012	2011	2012	2011
<b>Expenses</b>					
Amortization and depreciation		\$ 47,532	\$ 17,579	\$ 117,364	\$ 35,193
Bank charges and interest		1,327	( 2,227 )	4,875	940
Investor relations		20,923	22,697	130,079	98,454
Listing and filing fees		43,118	1,882	91,355	46,714
Office and sundry		53,874	37,216	175,028	110,967
Professional fees		57,610	69,352	169,294	165,006
Salaries and consulting fees		237,242	84,577	561,957	255,707
Stock-based compensation	6	-	23,788	1,650,069	1,453,829
Transfer agent fees		11,112	3,761	16,633	12,715
Travel and conference		29,597	40,312	150,917	146,842
<b>Loss before the undernoted</b>		<b>( 502,335 )</b>	<b>( 298,937 )</b>	<b>( 3,067,571 )</b>	<b>( 2,326,367 )</b>
<b>Other income (expenses)</b>					
Interest		45,633	-	76,481	217
Loss on foreign exchange		( 3,164 )	( 368 )	( 5,022 )	( 1,111 )
Part 12.6 tax expense		-	-	( 9,882 )	-
Amortization of flow-through premium liability		735,692	184,170	1,028,425	184,170
Flow-through share issuance expense		-	-	-	( 93,705 )
<b>Income (loss) before income taxes</b>		<b>275,826</b>	<b>( 115,135 )</b>	<b>( 1,977,569 )</b>	<b>( 2,236,796 )</b>
<b>Deferred tax expense</b>		<b>( 1,921,888 )</b>	<b>( 1,321,039 )</b>	<b>( 2,119,464 )</b>	<b>( 1,269,594 )</b>
<b>Net loss and comprehensive loss for the period</b>		<b>( 1,646,062 )</b>	<b>( 1,436,174 )</b>	<b>( 4,097,033 )</b>	<b>( 3,506,390 )</b>
<b>Basic and diluted loss per common share</b>					
		\$ ( 0.01 )	\$ ( 0.01 )	\$ ( 0.03 )	\$ ( 0.03 )
<b>Weighted average number of common shares outstanding</b>					
		157,825,379	121,989,130	135,355,786	103,098,810

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**Kivalliq Energy Corporation**  
*(An Exploration Stage Company)*  
**Condensed Statement of Changes in Equity**

*(Expressed in Canadian Dollars)*  
*Unaudited – Prepared by Management*

	Share Capital		Contributed surplus	Deficit	Total shareholders' equity
	Number of shares	Amount			
Balance, October 1, 2010	87,993,369	\$ 13,278,744	\$ 4,854,430	\$ (2,316,435)	\$ 15,816,739
Issued					
Private placements – non flow -through	10,300,000	5,150,000	-	-	5,150,000
Private placements – flow -through	19,476,457	12,144,948	-	-	12,144,948
Exercise of options	1,438,700	341,910	-	-	341,910
Exercise of w arrants	3,035,000	1,069,500	-	-	1,069,500
Fair value of options exercised	-	204,794	(204,794)	-	-
Fair value of w arrants exercised	-	412,923	(412,923)	-	-
Issued for resource property	250,000	85,000	-	-	85,000
Flow -through income tax renunciation	-	(1,125,000)	-	-	(1,125,000)
Stock-based compensation	-	-	1,430,041	-	1,430,041
Share issuance costs	-	(913,034)	204,271	-	(708,763)
Loss for the period	-	-	-	(2,070,216)	(2,070,216)
Balance, June 30, 2011	122,493,526	30,649,785	5,871,025	( 4,386,651 )	32,134,159
Issued					
Exercise of options	120,000	30,000	-	-	30,000
Fair value of options exercised	-	19,088	(19,088)	-	-
Flow -through income tax renunciation	-	(90,000)	-	-	(90,000)
IFRS adjustment to share capital on issuance of flow -through shares	-	330,557	-	-	330,557
Stock-based compensation	-	-	36,249	-	36,249
Share issuance costs – cash	-	(15,537)	-	-	(15,537)
Tax benefit on share issuance costs	-	250,714	-	-	250,714
Share issuance costs - w arrants	-	(182,613)	(21,658)	-	(204,271)
Loss for the period	-	-	-	(1,454,308)	(1,454,308)
Balance, September 30, 2011	122,613,526	30,991,994	5,866,528	( 5,840,959 )	31,017,563
Issued					
Private placements – non flow -through	20,251,444	9,113,150	-	-	9,113,150
Private placements – flow -through	23,617,900	10,628,055	-	-	10,628,055
Exercise of options	188,000	48,580	-	-	48,580
Exercise of w arrants	6,407,500	2,242,625	-	-	2,242,625
Fair value of options exercised	-	33,171	(33,171)	-	-
Fair value of w arrants exercised	-	921,514	(921,514)	-	-
Stock-based compensation	-	-	1,650,069	-	1,650,069
Share issuance costs - cash	-	(970,921)	-	-	(970,921)
Share issuance costs - w arrants	-	(332,579)	332,579	-	-
Tax benefit on share issuance costs	-	287,111	-	-	287,111
Loss for the period	-	-	-	(4,097,033)	(4,097,033)
<b>Balance, June 30, 2012</b>	<b>173,078,370</b>	<b>\$ 52,962,700</b>	<b>\$ 6,894,491</b>	<b>\$ (9,937,992)</b>	<b>\$ 49,919,199</b>

- The accompanying notes are an integral part of these condensed interim financial statements -

**Kivalliq Energy Corporation**  
*(An Exploration Stage Company)*  
**Condensed Statements of Cash Flows**

*(Expressed in Canadian Dollars)*  
*Unaudited – Prepared by Management*

	Three month periods ended June 30		Nine month periods ended June 30	
	2012	2011	2012	2011
<b>Cash Flows from Operating Activities</b>				
Net loss for the period	\$ (1,646,062)	\$ (1,436,174)	\$ (4,097,033)	\$ (3,506,390)
Adjustments for:				
Amortization and depreciation	47,532	17,579	117,364	35,193
Deferred tax recovery	1,921,888	1,321,039	2,119,464	1,269,594
Stock-based compensation	-	23,788	1,650,069	1,453,829
Flow-through share issuance expense	-	-	-	93,705
Amortization of flow-through premium liability	(735,692)	-	(1,028,425)	-
Interest income	(45,633)	-	(76,481)	(217)
Changes in non-cash working capital:				
Other receivables	(22,881)	-	397,200	2,543
HST recoverable	(256,640)	(74,985)	491,901	(148,817)
Prepaid expenses	142,195	(213,948)	60,728	48,880
Accounts payable and accrued liabilities	(236,142)	(1,117,325)	(126,990)	(1,104,813)
	(831,435)	(1,480,026)	(492,203)	(1,856,493)
Interest received	50,753	-	84,245	217
	(780,682)	(1,480,026)	(407,958)	(1,856,276)
<b>Cash Flows used in Investing Activities</b>				
Exploration and evaluation expenditures	(7,871,984)	914,882	(13,757,475)	(1,713,034)
Equipment and intangible assets	(73,411)	(140,805)	(322,274)	(151,497)
	(7,945,395)	774,077	(14,079,749)	(1,864,531)
<b>Cash Flows from Financing Activities</b>				
Issuance of share capital, net of issuance costs	10,853,092	11,546,364	22,286,830	17,184,024
	10,853,092	11,546,364	22,286,830	17,184,024
<b>Net Increase in Cash and Cash Equivalents</b>	<b>2,127,015</b>	<b>10,840,415</b>	<b>7,799,123</b>	<b>13,463,217</b>
Cash and Cash Equivalents - Beginning of Period	12,885,730	8,164,908	7,213,622	5,222,744
<b>Cash and Cash Equivalents - End of Period</b>	<b>\$ 15,012,745</b>	<b>\$ 19,005,323</b>	<b>\$ 15,012,745</b>	<b>\$ 18,685,961</b>

<b>Supplemental Schedule of Non-Cash Investing Activities</b>	<b>June 30, 2012</b>	<b>September 30, 2011</b>
Exploration and evaluation expenditures included in accounts payable	\$ 1,850,744	\$ 3,726,533

- The accompanying notes are an integral part of these condensed interim financial statements -

**Kivalliq Energy Corporation**  
*(An Exploration Stage Company)*  
**Schedule of Resource Property Costs**  
*(Expressed in Canadian Dollars)*  
*Unaudited – Prepared by Management*

	For the Nine month Period Ended June 30, 2012			For the year ended September 30, 2011
	Acquisition Costs	Deferred Exploration Costs	Total	Total
<b>Mineral Interests</b>				
<b>Angilak, Nunavut</b>				
Acquisition costs – shares and warrants	\$ -	\$ -	\$ -	\$ 85,000
Claim maintenance	147,985	-	<b>147,985</b>	179,118
Air support	-	4,424,215	<b>4,424,215</b>	6,178,564
Assays	-	270,099	<b>270,099</b>	223,346
Drilling	-	2,603,460	<b>2,603,460</b>	4,236,135
Field and general	-	1,898,970	<b>1,898,970</b>	1,710,102
Geological consulting	-	1,249,142	<b>1,249,142</b>	2,304,320
Travel and accommodation	-	1,287,815	<b>1,287,815</b>	1,342,973
<b>Resource Property Costs for the Period</b>	147,985	11,733,701	<b>11,881,686</b>	16,259,558
Balance, Beginning of the Period	836,032	27,046,439	<b>27,882,471</b>	11,622,913
<b>Balance end of the Period</b>	\$ 984,017	\$38,780,140	<b>\$ 39,764,157</b>	\$ 27,882,471

- The accompanying notes are an integral part of these condensed interim financial statements -

# **Kivalliq Energy Corporation**

*(An Exploration Stage Company)*

## **Notes to Condensed Interim Financial Statements**

**For the three and nine month periods ended June 30, 2012 and 2011**

*(Expressed in Canadian Dollars)*

*Unaudited – Prepared by Management*

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### **1. Nature of Operations and Going Concern**

Kivalliq Energy Corporation (“Kivalliq” or the “Company”) was incorporated as a wholly owned subsidiary of Kaminak Gold Corporation (“Kaminak”) on February 13, 2008 as 0816479 BC Ltd. under British Columbia’s Company Act. Effective February 20, 2008, 0816479 BC Ltd. changed its name to Kivalliq Energy Corp. Kivalliq is an exploration stage company focusing on the acquisition, exploration and development of resource properties.

Kivalliq became a reporting issuer in Alberta and British Columbia on July 4, 2008 by virtue of a reorganization transaction involving the exchange of securities between Kaminak, Kivalliq and the shareholders of Kaminak. The reorganization transaction involved the acquisition from Kaminak of a 100% interest in Kaminak’s Uranium properties (Angilak, Baker Lake and Washburn). On July 7, 2008, after completion of its private placements, Kivalliq’s shares became publicly trading on the TSX Venture Exchange under the symbol “KIV”.

Long-term continuance of Kivalliq’s operations is dependent upon achieving profitable operations and obtaining additional equity or debt financing. The recoverability of the carrying values of Kivalliq’s resource property interests is dependent upon the existence and discovery of economically recoverable reserves, the ability of Kivalliq to obtain the necessary financing to complete the development of these properties and future profitable production from or proceeds from the disposition of resource properties.

These condensed interim financial statements have been prepared on a going concern basis which assumes that Kivalliq will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The continuing operations of Kivalliq are dependent upon its ability to continue to raise adequate financing and to commence profitable operations in the future.

These condensed interim financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and balance sheet classifications that would be necessary were the going concern assumption deemed to be inappropriate. These adjustments could be material.

These condensed interim financial statements are unaudited, but in the opinion of management, reflect all adjustments (consisting of normal recurring accruals) necessary for fair presentation of the financial position, operations and changes in financial results for the interim periods presented.



# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

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### 2. Significant Accounting Policies

#### a) Basis of Presentation

These condensed interim financial statements have been prepared in accordance with International Accounting Standards (“IAS”) 34, *Interim Financial Reporting*, as issued by the International Accounting Standards Board (“IASB”). International Financial Reporting Standards (“IFRS”) 1, *First Time Adoption of IFRS* has been applied, as they are part of the period covered by Kivalliq’s first IFRS financial statements for the year ending September 30, 2012. The condensed interim financial statements do not include all of the information required for full annual financial statements. Kivalliq’s condensed interim financial statements were prepared in accordance with accounting principles generally accepted in Canada (“CGAAP”) until September 30, 2011. CGAAP differs from IFRS in some areas and accordingly, the significant accounting policies applied in the preparation of these condensed interim financial statements are set out below and have been consistently applied to all periods presented except in instances where IFRS 1 either requires or permits an exemption. The accounting policies followed in these condensed interim financial statements are the same as those applied in Kivalliq’s condensed interim financial statements for the period ended December 31, 2011. Any subsequent changes to IFRS that are reflected in Kivalliq’s financial statements for the year ending September 30, 2011 could result in the restatement of these condensed interim financial statements, including the transitional adjustments recognized as part of the IFRS accounting framework. An explanation of how the transition from CGAAP to IFRS has affected the reported statements of operations and comprehensive loss, financial position, and cash flows of Kivalliq is provided in note 12. This note includes information on the provisions of IFRS 1 and the exemptions that Kivalliq elected to apply, reconciliations of equity, net loss and comprehensive loss for comparative periods and equity at the date of transition, October 1, 2010.

These condensed interim financial statements should be read in conjunction with Kivalliq’s CGAAP annual financial statements for the year ended September 30, 2011, and Kivalliq’s condensed interim financial statements for the period ended December 31, 2011 prepared in accordance with IFRS applicable to interim financial statements.

#### b) Future Changes in Accounting Standards

A number of new standards, and amendments to standards and interpretations, are not yet effective for the period ended June 30, 2012, and have not been applied in preparing these condensed interim financial statements. None of these is expected to have a significant effect on the financial statements of Kivalliq, except for IFRS 9 Financial Instruments and IFRS 13 Fair Value Measurements, which become mandatory for Kivalliq’s 2015 and 2013 financial statements respectively. Kivalliq is in the process of evaluating these new standards and the impact has not yet been determined.

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 3. Equipment

	Furniture & Equipment	Computer Equipment	Field Equipment	Leasehold Improvements	Total
Cost at September 30, 2011	\$ 26,085	\$ 17,162	\$ 570,335	\$ 54,049	\$ 667,631
Additions	5,511	2,946	308,727	-	317,184
Cost at June 30, 2012	31,596	20,108	879,062	54,049	984,815
Accumulated depreciation at September 30, 2011	2,609	6,074	84,036	-	92,719
Depreciation	4,182	3,011	94,517	8,844	110,554
Accumulated depreciation at June 30, 2012	6,791	9,085	178,553	8,844	203,273
Net book value at June 30, 2012	\$ 24,805	\$ 11,023	\$ 700,509	\$ 45,205	\$ 781,542
Net book value at September 30, 2011	\$ 23,476	\$ 11,088	\$ 486,299	\$ 54,049	\$ 574,912

### 4. Intangible Assets

	Computer Software
Cost at September 30, 2011	\$ 24,891
Additions	5,090
Cost at June 30, 2012	29,981
Accumulated depreciation at September 30, 2011	19,770
Depreciation	6,810
Accumulated depreciation at June 30, 2012	26,580
Net book value at June 30, 2012	\$ 3,401
Net book value at September 30, 2011	\$ 5,121

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

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### 5. Exploration and Evaluation Assets

Details are as follows:

	Acquisition Costs	Exploration Costs	Cumulative as at June 30, 2012	Cumulative as at September 30, 2011
Angilak, Nunavut	\$ 984,017	\$38,780,140	\$ 39,764,157	\$ 27,882,471

#### General

Kivalliq acquired from Kaminak, a related party, through the reorganization transaction (Note 1) the Angilak Property.

#### Angilak, Nunavut

Angilak is a combination of two properties, located on Inuit Owned Lands and Federal Crown land in Nunavut.

Kaminak signed an Exploration Agreement (“EA”) with Nunavut Tunngavik Inc. (“NTI”) whereby Kaminak was granted a 100% interest in the minerals within privately owned Inuit Owned Lands. This parcel is located directly adjacent to Kaminak’s “Angilak (formerly Yathkyed) IOCG Project” which is comprised of staked claims located on Federal Crown land.

In order to keep the property in good standing, Kivalliq will agree to complete the following:

- Kivalliq will issue NTI 1,000,000 (issued) common shares from treasury staged over 36 months beginning after final TSX:V approval for the spin-out transaction.
- Upon completion of a feasibility study on any portion of the property, NTI has the option of taking either a 25% participating interest or a 7.5% net profits royalty in the specific area subject to the feasibility study.

Upon completion of a National Instrument 43-101 compliant report that outlines a measured resource of at least 12 million pounds of uranium, Kivalliq will pay NTI a cash sum of \$1,000,000.

As a consequence of the land claims settlement, the property is not subject to royalty obligations to the Government of Canada, but instead is subject to an underlying 12% net profits royalty payable on all minerals to NTI. During periods of positive operating revenue, gross uranium revenue shall be calculated as 130% of the value of the product. Starting December 31, 2008, Kivalliq will pay annual advanced royalty payments to NTI in the sum of \$50,000 annually (2008/2009/2010/2011 Paid).

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

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### 6. Share Capital

As at June 30, 2012, there were an unlimited number of common voting shares without par value authorized.

#### a) Private Placements

On May 29, 2012, Kivalliq closed a bought deal private placement of 16,772,900 flow-through common shares at a price of \$0.50 per flow-through common share and 7,124,000 non-flow-through common shares at a price of \$0.45 per non-flow-through common share for total gross proceeds of \$11,592,250.

In connection with this private placement Kivalliq issued 1,393,783 agent warrants exercisable at a price of \$0.45 per common share. Finder's fees consisted of cash payments of \$685,908 in commissions and \$20,000 in advisory fees. Kivalliq has recorded the fair value of these agent warrants as share issuance costs. The agent warrants attached to this issuance have been valued at \$253,898 based upon the Black-Scholes valuation model using the following assumptions noted below.

Risk-free interest rate	1.21%
Expected dividend yield	0%
Expected stock price volatility	91%
Average expected warrant life	2 years

On February 21, 2012, Kivalliq closed a non-brokered private placement of 13,127,444 common shares at a price of \$0.45 per common share, and 6,845,000 flow-through common shares at a price of \$0.52 per flow-through common share for gross proceeds of \$9,466,750.

In connection with this private placement Kivalliq issued 179,383 agent warrants exercisable at a price of \$0.50 per common share and 146,820 agent warrants exercisable at a price of \$0.55 per common share. Finder's fees consisted of cash payments of \$303,254. Kivalliq has recorded the fair value of these agent warrants as share issuance costs. The agent warrants attached to this issuance have been valued at \$78,681 based upon the Black-Scholes valuation model using the following assumptions noted below.

Risk-free interest rate	1.13%
Expected dividend yield	0%
Expected stock price volatility	93%
Average expected warrant life	2 years

On April 5, 2011, Kivalliq closed a non-brokered private placement of 1,750,000 common shares at a price of \$0.50 per common share for gross proceeds of \$875,000.

In connection with this private placement Kivalliq issued 60,000 finder warrants exercisable at a price of \$0.50 per common share. The finder warrants are exercisable for a period of two years from the date of issuance into one common share. The finder warrants attached to this issuance have been valued at \$18,116 based upon the Black-Scholes valuation model using the following assumptions noted below. Finder's fees of \$61,526 were paid in cash.

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

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### 6. Share Capital - Continued

#### a) Private Placements: - Continued

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Risk-free interest rate	1.86%
Expected dividend yield	0%
Expected stock price volatility	118%
Average expected warrant life	2 years

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On June 30, 2011, Kivalliq closed a non-brokered private placement of 8,550,000 common shares at a price of \$0.50 per common share for gross proceeds of \$4,275,000.

In connection with this private placement Kivalliq issued 249,000 finder warrants exercisable at a price of \$0.50 per common share. The finder warrants are exercisable for a period of two years from the date of issuance into one common share. The finder warrants attached to this issuance have been valued at \$75,237 based upon the Black-Scholes valuation model using the following assumptions noted below. Finder's fees of \$254,000 and due diligence and filing fees of \$20,076 were paid in cash.

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Risk-free interest rate	1.82%
Expected dividend yield	0%
Expected stock price volatility	118%
Average expected warrant life	2 years

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On March 30, 2011, Kivalliq closed a bought deal private placement of 12,333,600 flow-through common shares at a price of \$0.60 per flow-through common share for gross proceeds of \$7,400,160.

In connection with this private placement Kivalliq issued 370,008 agent warrants exercisable at a price of \$0.90 per common share. The agent warrants are exercisable for a period of two years from the date of issuance into one common share. The agent warrants attached to this issuance have been valued at \$89,260 based upon the Black-Scholes valuation model using the following assumptions noted below. Finder's fees of \$444,010 and due diligence and filing fees of \$28,959 were paid in cash.

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Risk-free interest rate	1.77%
Expected dividend yield	0%
Expected stock price volatility	118%
Average expected warrant life	2 years

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On December 20, 2010, Kivalliq closed a non-brokered private placement of 7,142,857 flow-through common shares at a price of \$0.70 per flow-through common share for gross proceeds of \$4,500,000. Finder's fees of \$120,000 were paid in cash.

The warrants attached to this issuance have been valued at \$1,223,357 based upon the Black-Scholes valuation model using the following assumptions noted below:

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 6. Share Capital - Continued

#### a) Private Placements: - Continued

Risk-free interest rate	1.38%
Expected dividend yield	0%
Expected stock price volatility	201%
Average expected warrant life	2 years

For all valuation models, the risk-free rate of return is the yield on a zero-coupon Canadian Treasury Bill of a term consistent with the assumed warrant life. The expected volatility is based on Kivalliq's historical prices. The expected average warrant is the average expected period to exercise, based on the historical activity patterns for warrants.

#### b) Warrants

Details as follows:

	Number of Warrants	Weighted Average Exercise Price
Outstanding warrants, October 1, 2010	20,285,000	\$0.36
Issued	679,008	\$0.72
Exercised	(3,035,000)	\$0.35
Outstanding warrants, September 30, 2011	17,929,008	\$0.38
Issued	1,719,986	\$0.46
Exercised	(6,407,500)	\$0.35
Expired	(2,042,500)	\$0.45
<b>Outstanding warrants, June 30, 2012</b>	<b>11,198,994</b>	<b>\$0.39</b>

At June 30, 2012, warrants enabling the holders to acquire common shares as follows:

Expiry Date	Weighted Average Exercise Price	Number of Warrants	Weighted Average Remaining Contractual Life in Years
July 28, 2012	\$0.35	6,350,000	0.08
September 10, 2012	\$0.35	2,450,000	0.20
March 30, 2013	\$0.90	370,008	0.75
March 31, 2013	\$0.50	249,000	0.75
April 5, 2013	\$0.50	60,000	0.76
February 21, 2014	\$0.50	179,383	1.65
February 21, 2014	\$0.55	146,820	1.65
May 29, 2014	\$0.45	1,393,783	1.91
<b>Weighted average of exercise price and remaining contractual life</b>	<b>\$0.39</b>	<b>11,198,994</b>	<b>0.42</b>

Refer to Note 13 for details of warrants exercised and expired subsequent to June 30, 2012.

## Kivalliq Energy Corporation

(An Exploration Stage Company)

### Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

#### 6. Share Capital - Continued

##### c) Stock Options

Under Kivalliq's stock option plan, the board of directors may grant options for the purchase of up to 10% of the total number of issued and outstanding common shares of Kivalliq. Options granted under the plan vest over time at the discretion of the board of directors and expire no later than five years from the date of issuance. Exercise prices on options granted under the plan cannot be lower than the market price of one share on the last trading day immediately preceding the day on which the option is granted, less the maximum applicable discount permitted by TSX Venture Exchange and the minimum exercise price per common share must be at least \$0.10.

The changes in stock options issued are as follows:

	Number of Options	Weighted Average Exercise Price
Outstanding options, October 1, 2010	5,730,200	\$0.26
Issued	2,945,000	\$0.51
Exercised	(1,558,700)	\$0.24
Cancelled	(14,000)	\$0.46
Outstanding options, September 30, 2011	7,102,500	\$0.37
Issued	5,700,000	\$0.50
Exercised	(188,000)	\$0.26
Cancelled	(569,500)	\$0.46
<b>Outstanding options, June 30, 2012</b>	<b>12,045,000</b>	<b>\$0.43</b>

At June 30, 2012 the following stock options were outstanding:

Expiry Date	Weighted Average Exercise Price	Issued Number of Options	Vested and Exercisable Number of Options	Weighted Average Remaining Contractual Life in Years
November 12, 2013	\$0.15	2,025,000	2,025,000	1.37
August 11, 2014	\$0.25	150,000	150,000	2.12
January 29, 2015	\$0.30	500,000	500,000	2.58
April 22, 2015	\$0.45	1,040,000	1,040,000	2.81
September 8, 2015	\$0.40	20,000	20,000	3.19
October 19, 2015	\$0.50	2,610,000	2,610,000	3.30
January 19, 2017	\$0.50	3,350,000	3,350,000	4.56
January 25, 2017	\$0.50	2,350,000	2,350,000	4.58
<b>Weighted average of exercise price and remaining contractual life</b>	<b>\$0.43</b>	<b>12,045,000</b>	<b>12,133,500</b>	<b>3.49</b>

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 6. Share Capital - Continued

#### a) Stock Options - Continued

Refer to Note 13 for details of options exercised subsequent to June 30, 2012.

During the nine month period ended June 30, 2012, Kivalliq granted options to acquire 5,700,000 common shares with a weighted average exercise price of \$0.50 per common share and a weighted average fair value of \$0.29 per option. Share-based compensation expense under the Black-Scholes option pricing model of \$1,650,069 (year ended September 30, 2011 - \$1,466,291) was recorded in relation to options vested during the period.

The fair value of stock options for all options issued was estimated at the grant date based on the Black-Scholes option pricing model with the following weighted average assumptions:

Risk-free interest rate	1.00%
Expected dividend yield	0%
Expected stock price volatility	107 - 108%
Expected forfeitures	0%
Average expected option life	2.5 years

During the year ended September 30, 2011, Kivalliq granted options to acquire 2,945,000 common shares with a weighted average exercise price of \$0.51 per common share, of which 2,926,250 vested during the year. The weighted average fair value of the options granted was \$0.48 per option for the year ended September 30, 2011.

The following weighted average assumptions were used for the valuation of stock options granted during the year ended September 30, 2011:

Risk-free interest rate	1.88%
Expected dividend yield	0%
Expected stock price volatility	175%
Expected forfeitures	0%
Average expected option life	5 years

For all valuation models, the risk-free rate of return is the yield on a zero-coupon Canadian Treasury Bill of a term consistent with the assumed warrant life. The expected volatility is based on Kivalliq's historical prices. The expected average warrant is the average expected period to exercise, based on the historical activity patterns for warrants. Expected forfeitures are based on historical forfeitures of Kivalliq's options.



# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 7. Related Party Transactions

#### *Key management compensation*

Key management consists of Kivalliq's directors and officers. In addition to management and consulting fees paid to these individuals, or companies controlled by these individuals, Kivalliq provides non-cash benefits. The aggregate value of compensation with key management for the nine month period ending June 30, 2012 was \$1,571,137 (2011 - \$1,475,312) and was comprised of the following:

	Nine month period ending June 30, 2012		Nine month period ending June 30, 2011	
Wages, salaries and consulting fees	\$	605,715	\$	358,080
Stock based compensation		946,505		1,097,741
Non-cash benefits		18,917		19,491
Total remuneration	\$	1,571,137	\$	1,475,312

#### *Related party transactions*

Related party transactions and balances not disclosed elsewhere in these condensed interim financial statements are as follows:

During the nine month period ended June 30, 2012, Kivalliq reimbursed \$294,315 (2011 - \$166,622) of rent, salaries, and office and administration expenses incurred by companies controlled by directors of Kivalliq.

During the nine month period ended June 30, 2012, Kivalliq reimbursed companies with common directors and key management \$163,093 (2011 - \$51,878) for travel and office costs incurred on behalf of Kivalliq.

During the nine month period ended June 30, 2012, Kivalliq incurred expenses on behalf of companies with common directors of \$27,837 for consulting and office expenses (2011 - \$nil).

The balance receivable from related parties at June 30, 2012 was \$35,457 (September 30, 2011 - \$308,270).

The balance payable to related parties at June 30, 2012 was \$70,173 (September 30, 2011 - \$110,455) and such payables are unsecured, non-interest bearing and are expected to be repaid under normal trade terms.

The amounts charged to Kivalliq for the services provided have been determined by negotiation among the parties and, in certain cases, are covered by signed agreements. These transactions were in the normal course of operations and were measured at the exchange value, which represented the amount of consideration established and agreed to by the related parties.

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

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### 8. Financial Instruments

#### Categories of financial assets and liabilities

The fair value of Kivalliq's cash and cash equivalents, other receivables, HST recoverable and accounts payable and accrued liabilities approximate carrying value which is the amount recorded on the balance sheet due to their short term nature.

#### *Credit risk*

Credit risk is the risk of loss associated with a counterparty's inability to fulfill its payment obligations. Kivalliq's credit risk is primarily attributable to other receivables. Management believes that the credit risk concentration with respect to financial instruments included in receivables is remote as receivables relate to interest receivable from a major financial institution, related party balances, HST recoverable from the Government of Canada, and other balances which have been subsequently collected.

#### *Liquidity risk*

Kivalliq's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at June 30, 2012, Kivalliq had a cash and cash equivalents balance of \$15,012,745 (September 30, 2011 - \$7,213,622) to settle accounts payable and accrued liabilities of \$1,898,525 (September 30, 2011 – \$3,901,304). All of Kivalliq's financial liabilities have contractual maturities of less than 30 days and are subject to normal trade terms. Management believes that Kivalliq has sufficient funds to meet its obligations as they become due.

#### *Market risk*

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices.

#### (a) Interest rate risk

Kivalliq has cash balances and no interest-bearing debt. Kivalliq's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. Kivalliq periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. As of June 30, 2012, Kivalliq had \$5,044,530 (September 30, 2011 – \$5,934,500) in term deposits.

#### (b) Foreign currency risk

Kivalliq operates predominately in Canada and is not exposed to any significant foreign currency risk.

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

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### 8. Financial Instruments - Continued

#### (c) Price risk

Kivalliq is exposed to price risk with respect to commodity and equity prices. Equity price risk is defined as the potential adverse impact on Kivalliq's earnings due to movements in individual equity prices or general movements in the level of the stock market. Commodity price risk is defined as the potential adverse impact on earnings and economic value due to commodity price movements and volatilities. Kivalliq closely monitors commodity prices of resources, individual equity movements, and the stock market to determine the appropriate course of action to be taken by Kivalliq.

### 9. Capital Management

Kivalliq's objectives when managing capital are to safeguard Kivalliq's ability to continue as a going concern in order to pursue the development of its resource properties and to maintain flexible capital structure for its projects for the benefit of its stakeholders.

In the management of capital, Kivalliq includes the components of shareholders' equity.

Kivalliq manages the capital structure and makes adjustments to it in light of changes in the economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, Kivalliq may attempt to issue new shares, enter into joint venture property arrangements, acquire or dispose of assets or adjust the amount of cash.

Management reviews the capital structure on a regular basis to ensure that the above-noted objectives are met. There were no changes in Kivalliq's approach to capital management during the nine month period ended June 30, 2012. Kivalliq is not subject to externally imposed capital requirements.

### 10. Commitments

Kivalliq has entered into agreements for the rental of office space that require minimum payments in the aggregate as follows:

Fiscal 2012	\$ 14,819
Fiscal 2013	59,276
Fiscal 2014	59,276
Fiscal 2015	59,276
Fiscal 2016	34,578
<b>Total Commitments</b>	<b>\$ 227,225</b>

### 11. Segment Information

Kivalliq operates in one reportable segment, being the acquisition, exploration and evaluation of mineral resources. All of Kivalliq's equipment and resource properties are located in Canada.

## **Kivalliq Energy Corporation**

*(An Exploration Stage Company)*

### **Notes to Condensed Interim Financial Statements**

**For the three and nine month periods ended June 30, 2012 and 2011**

*(Expressed in Canadian Dollars)*

*Unaudited – Prepared by Management*

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#### **12. First-Time Adoption of International Financial Reporting Standards (“IFRS”)**

Kivalliq adopted IFRS on October 1, 2011 with a transition date of October 1, 2010. Under IFRS 1 *First-time Adoption of International Financial Reporting Standards*, the IFRS are applied retrospectively at the transition date with all adjustments to assets and liabilities as stated under GAAP taken to retained earnings unless certain exemptions are applied. IFRS provides for certain optional exemptions and certain mandatory exceptions for first time IFRS adopters.

##### **a) *IFRS transition options***

Set forth below are the IFRS 1 applicable exemptions and exceptions applied in the conversion from Canadian GAAP to IFRS.

##### **Mandatory Exceptions**

In accordance with IFRS 1, an entity’s estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. Kivalliq’s IFRS estimates as of October 1, 2010 are consistent with its GAAP estimates for the same date.

##### **Optional Exemptions**

###### *Share-based payments*

IFRS 1 permits the application of IFRS 2 Share Based Payments only to equity instruments granted after November 7, 2002 that had not vested by the date of transition to IFRS. Kivalliq has applied this exemption and will apply IFRS 2 for equity instruments granted after November 7, 2002 that had not vested by October 1, 2010.

##### **b) *Reconciliations***

The adoption of IFRS has resulted in changes to Kivalliq’s reported financial position and results of operations. Kivalliq’s adoption of IFRS did not have an impact on the total operating, investing or financing cash flows. In order to allow the users of the financial statements to better understand these changes, the financial statements previously presented under Canadian GAAP have been reconciled to IFRS. For a description of the changes, see the discussion in notes to the IFRS reconciliations below.

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 12. First-Time Adoption of International Financial Reporting Standards (“IFRS”) - Continued

The Canadian GAAP Statement of Comprehensive (Loss) Income for the nine month period ended June 30, 2011 has been reconciled to IFRS as follows:

	Ref	(i)	(iii)	
	Canadian	Share-based	Flow-through Adj	IFRS
	GAAP	Compensation Adj		
<b>Expenses</b>				
Amortization and depreciation	\$ 35,193	\$ -	\$ -	\$ 35,193
Investor relations	98,454			98,454
Listing and filing fees	46,714			46,714
Office and sundry	111,907			111,907
Professional fees	165,006			165,006
Salaries and consulting fees	255,707			255,707
Stock-based compensation	1,485,338	(31,509)		1,453,829
Transfer agent fees	12,715			12,715
Travel and conference	146,842			146,842
Loss before other items	(2,357,876)	31,509	-	(2,326,367)
<b>Other Income (Expenses)</b>				
Interest	217			217
Loss on foreign exchange	(1,111)			(1,111)
Flow through share issuance expense	-		(93,705)	(93,705)
Amortization of Flow through share premium liability	-		184,170	184,170
Loss For the Period Before Taxes	(2,358,770)	31,509	90,465	(2,236,796)
Deferred Income Tax Recovery (Expense)	243,761		(1,513,355)	(1,269,594)
Net Loss For The Period	(2,115,009)	31,509	(1,422,890)	(3,506,390)
Deficit - beginning of period	(2,269,822)	(46,613)		(2,316,435)
Deficit - end of period	\$ (4,384,831)	\$ (15,104)	\$ (1,422,890)	\$ (5,822,825)

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 12. First-Time Adoption of International Financial Reporting Standards (“IFRS”) - Continued

The Canadian GAAP Statement of Comprehensive (Loss) Income for the three month period ended June 30, 2011 has been reconciled to IFRS as follows:

	Ref	(i)	(iii)	
	Canadian	Share-based	Flow-through Adj	IFRS
	GAAP	Compensation Adj		
<b>Expenses</b>				
Amortization and depreciation	\$ 17,579	\$ -	\$ -	\$ 17,579
Investor relations	22,697			22,697
Listing and filing fees	1,882			1,882
Office and sundry	34,989			34,989
Professional fees	69,352			69,352
Salaries and consulting fees	84,577			84,577
Stock-based compensation	13,593	10,195		23,788
Transfer agent fees	3,761			3,761
Travel and conference	40,312			40,312
Loss before other items	(288,742)	(10,195)	-	(298,937)
<b>Other Income (Expenses)</b>				
Loss on foreign exchange	(368)			(368)
Amortization of Flow through share premium liability	-		184,170	184,170
Loss For the Period Before Taxes	(289,110)	(10,195)	184,170	(115,135)
Deferred Income Tax Recovery (Expense)	68,880		(1,389,919)	(1,321,039)
Net Loss For The Period	(220,230)	(10,195)	(1,205,749)	(1,436,174)
Deficit - beginning of period	(4,164,601)	(4,909)	(217,141)	(4,386,651)
Deficit - end of period	\$ (4,384,831)	\$ (15,104)	\$ (1,422,890)	\$ (5,822,825)

# Kivalliq Energy Corporation

(An Exploration Stage Company)

## Notes to Condensed Interim Financial Statements

For the three and nine month periods ended June 30, 2012 and 2011

(Expressed in Canadian Dollars)

Unaudited – Prepared by Management

### 12. First-Time Adoption of International Financial Reporting Standards (“IFRS”) - Continued

The June 30, 2011 Canadian GAAP Statement of Financial Position has been reconciled to IFRS as follows:

	Ref	(i)	(ii)	(iii)	
	Canadian GAAP	Share-based	Software	Flow-through Adj	IFRS
	Jun 30 2011	Compensation Adj	reclassification		Jun 30 2011
<b>Assets</b>					
<b>Current</b>					
Current assets	\$ 16,693,774	\$ -	\$ -	\$ -	\$ 16,693,774
Equipment	203,326		(6,032)		197,294
Intangible assets	-		6,032		6,032
Exploration and Evaluation Assets	19,791,899				19,791,899
	<b>36,688,999</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>36,688,999</b>
<b>Liabilities And Shareholders' Equity</b>					
Accounts payable and accrued liabilities	3,079,394				3,079,394
Flow through share premium liability				1,049,190	1,049,190
Deferred tax liability	1,429,539			388,355	1,817,894
	4,508,933	-	-	1,437,545	5,946,478
<b>Shareholders' equity</b>					
Share capital	30,664,439			(14,655)	30,649,784
Contributed surplus	5,900,458	15,104			5,915,562
Deficit	(4,384,831)	(15,104)		(1,422,890)	(5,822,825)
	32,180,066	-	-	(1,437,545)	30,742,521
	<b>\$ 36,688,999</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 36,688,999</b>

## **Kivalliq Energy Corporation**

*(An Exploration Stage Company)*

### **Notes to Condensed Interim Financial Statements**

**For the three and nine month periods ended June 30, 2012 and 2011**

*(Expressed in Canadian Dollars)*

*Unaudited – Prepared by Management*

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#### **12. First-Time Adoption of International Financial Reporting Standards (“IFRS”) - Continued**

##### **Notes to the IFRS reconciliations:**

##### *i) Share-based payments*

Under Canadian GAAP, the fair value of stock-based awards with graded vesting are calculated as one grant and the resulting fair value is recognized on a straight-line basis over the vesting period. Forfeitures of awards are recognized as they occur.

Under IFRS, a fair value measurement is required for each vesting instalment within the option grant. Each instalment must be valued separately, based on assumptions determined from historical data, and recognized as compensation expense over each instalment's individual tranche vesting period. Forfeiture estimates are recognized in the period they are estimated, and are revised for actual forfeitures in subsequent periods. As at June 30, 2011, and for the nine month period then ended, this accounting policy change resulted in an increase in contributed surplus of \$15,104, an increase in deficit of \$15,104, and a decrease of \$31,509 in share-based compensation expense. For the three month period ended June 30, 2011, this accounting policy change resulted in an increase of \$10,195 in share-based compensation expense.

##### *ii) Software reclassification*

Under Canadian GAAP, Kivalliq carries its computer software in equipment.

Under IFRS, when computer software is not an integral part of the related hardware, computer software is treated as an intangible asset. Accordingly, Kivalliq has reclassified its computer software (none of which is considered an integral part of the related hardware) from equipment to intangible assets. As at June 30, 2011, this accounting policy change has resulted in a \$6,032 decrease in the carrying value of equipment and a corresponding increase in the carrying value of intangible assets.

##### *iii) Flow-through shares*

The treatment of the tax effect of flow-through shares differs under Canadian GAAP and IFRS.

Under Canadian GAAP, share capital is recorded at net proceeds less the deferred tax liability related to the renounced expenditures.

Under IFRS, the amount recorded to share capital when flow-through shares are issued is measured based on the current market price of common shares. The incremental proceeds, or "premium", are recorded as a liability. When qualifying expenditures are incurred and the intention is to renounce the tax benefit to the shareholders, the flow-through share premium is recognized in other income and the liability is reversed. When the expenditures from the flow-through shares are renounced, a deferred tax expense is recognized with a corresponding deferred tax liability being recorded. The deferred tax liability and expense is eliminated to the extent that Kivalliq can recognize previously unrecognized deferred tax assets to offset the liability.



## **Kivalliq Energy Corporation**

*(An Exploration Stage Company)*

### **Notes to Condensed Interim Financial Statements**

**For the three and nine month periods ended June 30, 2012 and 2011**

*(Expressed in Canadian Dollars)*

*Unaudited – Prepared by Management*

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#### **12. First-Time Adoption of International Financial Reporting Standards (“IFRS”) - Continued**

##### **Notes to the IFRS reconciliations:**

##### *iii) Flow-through shares - Continued*

As at June 30, 2011, and for the nine month period then ended, this accounting policy change resulted in an increase in the flow-through share premium liability of \$1,049,190, an increase in the deferred tax liability of \$388,355, a decrease in share capital of \$14,655, an increase in deficit of \$1,422,890, an increase in flow-through share issuance expense of \$93,705, an increase in amortization of flow-through share premium liability of \$184,170, and an increase in deferred tax expense of \$1,513,355. For the three month period ended June 30, 2011, this accounting policy change resulted in an increase in amortization of flow-through share premium liability of \$184,170 and an increase in deferred tax expense of \$1,389,919.

#### **13. Subsequent Events**

- a) Subsequent to June 30, 2012, 70,000 options were exercised for gross proceeds of \$10,500.
- b) Subsequent to June 30, 2012, 200,000 warrants were exercised for gross proceeds of \$70,000 and 6,350,000 warrants expired without exercise.